CLERK'S COPY.

TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 180

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

DONALD H. OWENS AND MARION HAVILAND OWENS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED JULY 6, 1938
CERTIORARI GRANTED OCTOBER 10, 1938

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 180

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

VS.

DONALD H. OWENS AND MARION HAVILAND OWENS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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194408—38——1

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 86479

ONALD H. OWENS AND MARION HAVILAND OWENS (HUSBAND AND WIFE), PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For Taxpayers: Robert N. Miller, Esq., Ewing verett, Esq., O. H. Chmillon, Esq. For Commissioner: Harry orrow, Esq.

Docket entries

1936	
ept.	9—Petition received and filed. Taxpayer notified. (Fee paid.)
"	9—Copy of petition served on General Counsel.
ct.	28—Answer filed by General Counsel.
"	30—Copy of answer served on taxpayer.
1937	
an.	14—Hearing set February 15, 1937.
eb.	15—Hearing had before Mr. Arundell, Div. 7, on merits. Stipulation of facts (2) filed. Petitioner's brief due 4/1/37—respondent's brief due 5/1/37—petitioner's reply 5/17/37.
lar.	23—Transcript of hearing of February 15, 1937 filed.
"	26—Brief filed by taxpayer. 3/27/37 copy served.
pr.	17—Brief filed by General Counsel.
lay	26—Memorandum Findings of Fact and Opinion entered, Mr. Arundell, Div. 7. Decision will be entered for the petitioner.
"	26—Decision entered, Mr. Arundell, Div. 7.
ng.	19—Petition for review by U. S. Circuit Court of Appeals (2) with assignments of error filed by General Counsel.
"	28—Proof of service filed by General Counsel. (2). Counsel.
ept.	1—Proof of service on counsel for taxpayer filed by General
"	28—Praecipe with proof of service thereon filed by General Counsel.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted.]

Petition

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:A 2:AEF-90D) dated August 29, 1936, and, as a basis for their proceeding, allege as follows:

1. The petitioners are husband and wife whose mailing address is: c/o Bram, Wrightson & Co., 99 John Street, New York City, New York.

2. The notice of deficiency (a copy of which is attached hereto as Exhibit A) was mailed to petitioners on August 29, 1936.

3. The taxes in controversy are income and surtaxes for the calendar year 1934 and in the amount of $336.00.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) Respondent erred in determining the net taxable income of petitioner, Donald H. Owens, for the calendar year 1934 in failing and refusing to allow as a deduction the sum of $1,600.00 representing a loss sustained by said petitioner on account of the wrecking of his automobile during said calendar year.

(b) Respondent erred in determining that the deductible loss sustained by petitioner, Donald H. Owens, on account of the wrecking of his automobile during the calendar year 1934 did not exceed the sum of $35.00.

(c) Respondent erred in determining a deficiency in tax in the amount of $336.00 against petitioners for the calendar year 1934.

5. The facts upon which petitioners rely as the basis of this proceeding are as follows:

(a) Petitioners, Donald H. Owens and Marion Haviland Owens, are husband and wife and filed a joint income tax return for the calendar year 1934.

(b) Prior to 1934, petitioner had purchased a Nash touring automobile at a cost to him of $1,825.00 which until June 1934 was used by him for personal uses only and was not used in connection with any trade or business carried on by petitioner.

(c) That petitioner did not claim and was not allowed any deduction on account of depreciation of said Nash automobile during any taxable year, nor was a depreciation deduction allowable under the law with respect thereto.

(d) That in June, 1934, by reason of an accidental collision with another automobile, the petitioner's automobile was wrecked and partially demolished and thereafter had a fair market value of $190.00.

(e) That by reason of said accidental collision between the automobile owned by petitioner with another automobile, petitioner sustained a loss of $1,635.00 representing the difference between the cost

to petitioner of his automobile, $1,825.00, and its fair market value after said accidental collision, $190.00.

(f) That petitioner did not at the time of said accident in June, 1934, carry any insurance on his automobile and petitioner has not received any compensation through insurance or otherwise for any of the loss sustained by reason of said accident.

(g) That in determining the taxable net income of petitioners for the calendar year 1934, petitioner, Donald H. Owens, claimed as a loss under Section 23 (e) (2) of the Revenue Act of 1934 the sum of $1,635.00 on account of the accidental collision of his automobile as aforesaid.

(h) That petitioner, in determining said deduction, used as
6 a basis the cost to him of said automobile as provided under Section 23 (h) and 113 (b) of the Revenue Act of 1934.

(i) That under the above cited provisions of the Revenue Act of 1934, the loss on account of the accidental wrecking and partial demolition of petitioner's automobile deductible in determining petitioner's taxable net income for the calendar year 1934 is $1,635.00.

(j) That respondent, in determining petitioner's taxable net income for the calendar year 1934 has allowed as a loss due to the accidental wrecking of petitioner's automobile the sum of $35.00 representing the difference between the fair market value of said automobile in June, 1934, before the accident, $225.00, and the fair market value thereof after the accident, $190.00; and has failed and refused to allow as a deduction any sum in excess of said $35.00.

Wherefore, petitioners pray that this Board may hear the proceeding and determine:

(a) That petitioner, Donald H. Owens, sustained a loss of $1,635.00 on account of the accidental wrecking of his automobile which loss is deductible in determining petitioners' taxable net income for the calendar year 1934.

(b) That there is no deficiency in income tax due from petitioners for the calendar year 1934; and

7 (c) Grant such other and further relief to which petitioners are entitled in law or equity.

(Sd) ROBERT N. MILLER,
Robert N. Miller,
920 Southern Bldg., Washington, D. C.
(Sd) EWING EVERETT,
Ewing Everett,
20 Exchange Place, New York, N. Y.
(Sd) O. H. CHMILLON,
O. H. Chmillon,
920 Southern Bldg., Washington, D. C.
Attorneys for Petitioners.

8 [*Duly sworn to by Donald H. Owens and Marion H. Owens; jurat omitted in printing.*]

Exhibit A, to foregoing petition

AUGUST 29, 1936.

IT:A 2
AEF—90D
Mr. DONALD H. OWENS and
Mrs. MARION HAVILAND OWENS
(Husband and Wife),
% Ream Wrightson & Co., 99 John Street,
New York, New York.

SIR AND MADAM: You are advised that the determination of your income tax liability for the taxable year 1934 discloses a deficiency of $336.00, as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C. for the attention of IT:C:P-7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period
10 terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner.
By W. T. SUMNWOOD,
Acting Deputy Commissioner.

Enclosures: Statement.
Form 870.
AEF/WGH—2.

STATEMENT

IT:A 2
AEF—90D.

In re: Mr. Donald H. Owens and Mrs. Marion Haviland Owens (Husband and Wife), % Ream, Wrightson & Co., 99 John St., New York, N. Y.

INCOME TAX LIABILITY

Year, 1934; income tax liability, $2,946.55; income tax assessed, $2,610.55; deficiency, $336.00.

The deficiency shown herein is based on the report dated
11 January 27, 1936, prepared by Revenue Agent Kenneth B.

Dyer, a copy of which has been furnished you and on information furnished in your protest and at the conference held in the agent's office on July 21, 1938.

You are advised that your net income and tax liability have been adjusted as follows:

Net income as shown on return	$25,978.85
Add: Deduction disallowed	1,600.00
Net income as adjusted	$27,578.85
Personal exemption	2,000.00
Amount subject to surtax	$24,678.85
Earned income credit	1,400.00
Amount subject to normal tax	$23,278.85
Normal tax of 4% on $23,278.85	931.15
Surtax on $24,678.85	2,015.40
Correct tax liability	$2,946.55
Tax previously assessed, a/c No. 222214	2,610.55
Deficiency in tax	$336.00

EXPLANATION OF CHANGE

The deduction of $1,635.00 claimed as a loss on account of the wreck of a touring car has been decreased to $35.00 and the difference or $1,600.00 disallowed. You are advised that careful con-
12 sideration has been given to all the information furnished relative to this item. However, this office holds that the deduction allowable under section 23 (e) (3) of the Revenue Act of 1934 is the amount of loss actually sustained based on the value of the car at the time of the accident. Since this value has been determined to be $225.00 and the salvage value was $190.00, the difference or $35.00 is held to be an allowable deduction from your net income.

The adjustment of this item indicates a deficiency in tax amounting to $336.00 as explained above.

A copy of this communication has been forwarded to your representative, Mr. Ewing Everett, 48 Wall Street, New York, New York, who has on file in this office a duly recorded power of attorney.

AEF/WGH—2

13 BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted.]

Answer

The Commissioner of Internal Revenue, by his attorney, Herman Oliphant, General Counsel for the Department of the Treasury, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.
2. Admits the allegations contained in paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4. Denies that the respondent erred as alleged in subparagraph (a) to (c), both inclusive, of paragraph 4 of the petition.

5. (a). Admits the allegations contained in subparagraph 5 (a).

(b). Admits that the petitioner purchased a Nash automobile; denies all remaining allegations contained in subparagraph 5 (b) of the petition.

(c), (d). Admits the allegations contained in subparagraph 5 (c) and 5 (d) of the petition.

(e), (f). Denies the allegations contained in subparagraph 5 (e) and 5 (f) of the petition.

(g). Admits the allegations contained in subparagraph 5 (g).

(h), (i). Denies the allegations contained in subparagraphs 5 (h) and 5 (i) of the petition.

(j). Admits the allegations contained in subparagraph 5 (j) of petition.

Denies that the petitioner is entitled to the relief prayed for in the petition.

Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that taxpayer's appeal be denied.

(Signed) HERMAN OLIPHANT,
Herman Oliphant,
General Counsel for the Department of the Treasury,
Of Counsel.

HARRY R. HORROW,
Special Attorney,
Bureau of Internal Revenue.

15 BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 86479

DONALD H. OWENS AND MARION HAVILAND OWENS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

The amount of loss arising from casualty determined.

O. H. Chmillon, Esq., for the petitioners.
Harray Horrow, Esq., for the respondent.

Memorandum findings of fact and opinion

ARUNDELL: This is a proceeding for the redetermination of a deficiency in income taxes for the year 1934, in the amount of $336.

This proceeding involves only the determination of the amount of loss sustained by reason of damage to an automobile resulting from an accidental collision in 1934.

The facts were stipulated and briefly are as follows:

Findings of fact

The petitioners are husband and wife. Prior to January 1,
16 1934, but after March 1, 1913, the petitioner, Donald H. Owens, purchased a Nash touring automobile at a cost to him of $1,825, which automobile at all times since has been and was until June 1934, used by him for his personal use only and not in connection with any trade or business carried on by him. In June 1934, by reason of an accidental collision with another automobile, the automobile was wrecked and partly demolished. It thereafter had a fair market value of $190. Immediately prior to such collision, the automobile had a fair market value of $225. He carried no insurance on the automobile and has not received any compensation through insurance or otherwise for any part of the loss sustained by reason of the accident.

The petitioner and his wife filed a joint income tax return for the calendar year 1934. No deduction on account of depreciation of the automobile was claimed or allowed during any taxable year. In the return for 1934 filed by the petitioners a loss deduction was claimed in the amount of $1,635, being the difference between the cost and the salvage value of the automobile immediately after the accident. The respondent allowed a deduction in the amount of $35, representing the difference between the fair market value of the automobile immediately prior to the accident and its salvage value immediately after the accident.

Opinion

The facts herein are not in dispute. The respondent con-
17 cedes that the petitioners sustained a loss as a result of the collision of the Nash automobile with another automobile and that the amount of the loss sustained is deductible under section 23 (e) (3) (1) of the Revenue Act of 1934. However, the parties disagree as to the amount of the loss.

The petitioners contend that the loss sustained was a complete loss except for the salvage remaining after the collision and that consequently they sustained a loss in the amount of the difference between the cost of the automobile and the salvage value after the

(1) Sec. 23.
In computing net income there shall be allowed as deductions:
* * * * * * * *
(e) Losses by Individuals.—In the case of an individual losses sustained during the taxable year and not compensated for by insurance or otherwise—
* * * * * * * *
(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. * * *

collision. The applicable sections of the Revenue Act of 1934 are set forth in the margin. Sections 23 (h) (²), 113 (a) and 18 (b) (³), and 111 (a) (⁴). It is apparent from the stipulation of the parties, to the effect that the automobile was wrecked and partly demolished so that a salvage value only remained, that a complete loss resulted except for the value of the salvage remaining after the collision. Section 23 (h), supra, provides that the basis for determining a loss from casualty shall be the "cost." Therefore, the deductible amount of the loss sustained by petitioners is the difference between cost and the salvage value. Francis M. Bass, 30 B. T. A. 4, E. C. O'Bear, 28 B. T. A. 698, affirmed 80 Fed. (2d) 473; Ferguson v. Commissioner, 59 Fed. (2d). 803; and Pioneer Cooperage Co., 53 Fed. (2d). 43, affirming 17 B. T. A. 119, Certiorari denied, 284 U. S. 686. The case of Harry Johnston Grant, 30 B. T. A. 1028, cited by the respondent, involved the determination of the amount of a partial loss due to casualty. Therein a residence property was damaged by the sinking of a portion of the land without 19 physical damage to the building thereon or the remaining land. The formula used therein to determine the amount of such partial loss under the factual situation presented therein is not applicable in determining the amount of a loss where there is a complete destruction or loss except for some salvage of little value, as herein involved.

The respondent contends that the amount of the loss is the difference between the value before and the value immediately after the casualty. A similar contention was made by a taxpayer in Pioneer Cooperage Co., supra, wherein the Board stated as follows:

* * * To carry petitioner's contention to its logical conclusion would be quite disturbing to the taxpayers of the country. It would deny to them deductions for actual losses where their property had fallen in value. If petitioner's property had decreased in value instead of having increased, we seriously doubt whether it would persist in its present condition. Yet, if one's deductible loss is to be measured by the market value of property at the date of loss, when the property increases in value, by the same token it should be measured by

---

(²) Sec. 23.

(h) Basis for Determining Loss.—The basis for determining the amount of deduction for losses sustained, to be allowed under subsection (e) or (f), shall be the adjusted basis provided in section 113 (b) for determining the loss from the sale or other disposition of property.

(³) Sec. 113. Adjusted Basis for Determining Gain or Loss.

(a) Basis (Unadjusted) for Property.—The basis of property shall be the cost of such property; except (that—[Exceptions not applicable here].

* * * * * * *

(b) Adjusted Basis.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) General Rule.—Proper adjustment in respect of the property shall in all cases be made—

* * * * * * *

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws. * * *

(⁴) Sec. 111. Determination of Amount of, and Recognition of, Gain or Loss.

(a) Computation of Gain or Loss.—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

the same standard when it has shrunken in value. To apply the rule contended for by petitioner would be to grant deductible losses only where the property had value when lost, and then only to the extent of its then present value, and thus disregard all question of cost or value at date of acquisition. * * *

20 * * * To put it another way, is petitioner entitled to take as a loss an amount, part of which cost him nothing but which is in the nature of unrealized income, or only that amount which it is actually out of pocket?"

The action of the respondent in disallowing the loss claimed in full is, therefore, disapproved.

Enter:

Decision will be entered for the petitioners.

(Entered May 26, 1937)

Before United States Board of Tax Appeals, Washington

Docket No. 86479

DONALD H. OWENS AND MARION HAVILAND OWENS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to the determination of the Board, as set forth in its Memorandum Findings of Fact and Opinion entered May 26, 1937, it is

21 Ordered and decided: That there is no deficiency in income tax for the year 1934.

Enter:

[SEAL] (Signed) O. ROGERS ARUNDELL,
Member.

(Entered May 26, 1937)

In United States Circuit Court of Appeals for the Second Circuit

[Title omitted.]

Petition for review and assignments of error

To the Honorable JUDGES OF THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT:

Now comes Guy T. Helvering, Commissioner of Internal Revenue, by his attorneys, James W. Morris, Assistant Attorney General, Morrison Shafroth, Chief Counsel, Bureau of Internal Revenue, and Harry R. Horrow, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

22

I

JURISDICTION

The petitioner on review (hereinafter referred to as the Commissioner) is the duly appointed, qualified, and acting Commissioner of Internal Revenue of the United States, holding his office under and by virtue of the laws of the United States. The respondents on review (hereinafter referred to as the taxpayers) are individuals with their residence in Chappaqua, New York.

The return of the taxpayers for the year 1934 was made to the Collector of Internal Revenue for the Second District of New York, at New York, N. Y., whose office is located in the judicial district of the United States Circuit Court of Appeals for the Second Circuit.

II

NATURE OF CONTROVERSY

On August 29, 1936, the Commissioner, pursuant to the provisions of section 272 (a) of the Revenue Act of 1934 (48 Stat. 741; U. S. C. Tit. 26, sec. 272), forwarded to the taxpayers, by registered mail, a notice of deficiency wherein the taxpayers were notified of the Commissioner's determination of a deficiency of $336.00 in the taxpayers' income tax liability for the year 1934.

23 Thereafter on September 9, 1936, the taxpayers filed their petition with the United States Board of Tax Appeals for a redetermination of the proposed deficiency in their income tax liability for the year 1934 as disclosed by the notice of deficiency, dated August 29, 1936, as aforesaid, which petition was assigned Docket No. 86479. On October 23, 1936, the Commissioner filed with the Board of Tax Appeals his answer to the petition so filed by the taxpayers. The proceeding came on for hearing before a division of the Board of Tax Appeals sitting at Washington, D. C., on February 15, 1937, and was submitted on a stipulation of facts.

The taxpayers are husband and wife. Prior to January 1, 1934, but after March 1, 1913, one of the taxpayers, Donald H. Owens, purchased an automobile at a cost of $1,825.00, which automobile at all times since and until June 1934, was used by him for his personal use only and not in connection with any trade or business carried on by him. In June 1934, by reason of an accidental collision with another automobile, the aforesaid automobile was wrecked and partly demolished. Immediately prior to such accident, the automobile had a fair market value of $225.00, and thereafter it had a fair market value of $180.00. The taxpayer has received no compensation through insurance or otherwise for any part of the loss sustained by reason of said accident.

The taxpayers filed a joint income tax return for the calendar year 1934. No deduction on account of depreciation of the automobile was claimed or allowed during any taxable year. On
24 the return filed for 1934, the taxpayers claimed a deduction in the amount of $1,635.00 on account of the alleged loss sustained by reason of the aforesaid accident. Said deduction represented the difference between the original cost of the automobile and its salvage value immediately after the accident. The Commissioner, in determining the deficiency involved in this proceeding did not allow the full amount of the deduction claimed but allowed a deduction in the amount of $35.00, representing the difference between the fair market value of the automobile immediately prior to the accident and its salvage value immediately thereafter.

On May 26, 1937, the Board of Tax Appeals promulgated its memorandum opinion wherein it was held that the Commissioner erred in failing to allow the full amount of the deduction claimed by the taxpayers. On May 26, 1937, the Board entered its judgment wherein it was ordered and decided that there is no deficiency in income tax for the year 1934.

There is no dispute that the taxpayers sustained a loss which is allowable as a deduction under section 23 (e) (3) of the Revenue Act of 1934 (48 Stat. 689; U. S. C. Tit. 26, sec. 23 [e[[3]). The sole question presented is whether such deduction is measured by the actual loss sustained; namely, the difference between the fair market value of the automobile immediately prior to the accident and its salvage value, as contended by the Commissioner, or by the difference between the original cost of the automobile and its salvage value after the accident, as contended by the taxpayers.

25

III

ASSIGNMENTS OF ERROR

The Commissioner, being aggrieved by the action of the Board of Tax Appeals in the proceeding, desires to obtain a review of its aforesaid decision by the United States Circuit Court of Appeals for the Second Circuit, and alleges as grounds for such review that the Board of Tax Appeals committed the following errors:

1. The Board erred in deciding that there is no deficiency in income tax due from the taxpayers for the year 1934.

2. The Board erred in failing to decide that there is a deficiency in income tax due from the taxpayers for the year 1934 in the amount of $336.00.

3. The Board erred in holding that the Commissioner erred in failing to allow the taxpayers a deduction for the year 1934 in the amount of $1,635.00 by reason of a loss sustained with respect to an automobile used for personal purposes.

4. The Board erred in failing to hold that the deduction allowable to the taxpayers for such loss for the year 1934 is not in excess of $35.00, the amount allowed by the Commissioner in determining the deficiency involved herein.

5. The Board erred in holding and deciding that the amount
26 of the deduction allowable to the taxpayers for such loss is the difference between the original cost of the automobile and its salvage value.

6. The Board erred in failing to hold and decide that the amount of the deduction allowable to the taxpayers for such loss is the difference between the fair market value of the automobile immediately before its partial destruction and its salvage value.

Wherefore, the Commissioner petitions that the aforesaid decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Second Circuit; that a transcript of record be prepared in accordance with law and the rules of said Court and transmitted to the Clerk of said Court for filing; and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by said Court.

(Signed) JAMES W. MORRIS,
Assistant Attorney General.

(Signed) MORRISON SHAFROTH,
Morrison Shafroth,
Chief Counsel,
Bureau of Internal Revenue.

(Signed) HARRY R. HORROW,
Harry R. Horrow,
Special Attorney,
Bureau of Internal Revenue.

27 [*Duly sworn to by Harry R. Horrow; jurat omitted in printing.*]

28 In United States Circuit Court of Appeals

[Title omitted.]

Notice of filing petition for review

To:

DONALD H. OWENS,
% Ream, Wrightson & Co., 99 John Street, New York, N. Y.

MARION HAVILAND OWENS,
% Ream, Wrightson & Co., 99 John Street, New York, N. Y.

You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of August 1937, file with the Clerk of

the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore
29 rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 19th day of August 1937.

(Signed) MORRISON SHAFROTH,
Morrison Shafroth,
Chief Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 23rd day of August 1937.

(Sgd.) DONALD H. OWENS,
(Sgd.) MARION HAVILAND OWENS,
Respondents on Review.

30 In United States Circuit Court of Appeals

[Title omitted.]

Notice of filing petition for review

To EWING EVERETT, Esq.,
20 Exchange Place, New York, N. Y.

You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of August 1937, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 19th day of August 1937.

(Signed) MORRISON SHAFROTH,
Morrison Shafroth,
Chief Counsel,
Bureau of Internal Revenue.

31 Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 20th day of August 1937.

(Sgd.) EWING EVERETT,
Attorney for Respondents on Review.

In United States Circuit Court of Appeals

[Title omitted.]

Notice of filing petition for review

To:

ROBERT N. MILLER,
920 Southern Building, Washington, D. C.
O. H. CHAMBLISS,
920 Southern Building, Washington, D. C.

32 You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of August 1937, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Second Circuit of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 19th day of August 1937.

(Signed) MORRISON SHAFROTH,
Morrison Shafroth,
Chief Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 20th day of August 1937.

(Sgd.) ROBERT N. MILLER,
(Sgd.) O. H. CHAMBLISS,
Attorneys for Respondents on Review.

33 In United States Circuit Court of Appeals

[Title omitted.]

Praecipe for record

To the CLERK OF THE UNITED STATES BOARD OF TAX APPEALS:

You will please prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Second Circuit copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Second Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.
2. Pleadings before the Board.
   (a) Petition, including annexed copy of notice of deficiency.
34 (b) Answer.
3. Memorandum findings of fact and opinion of the Board.

4. Decision of the Board.
5. Petition for review.
6. Notices of filing petition for review.
7. This praecipe.

(Sgd.) J. P. Wenchel,
J. P. Wenchel,
Chief Counsel,
Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 24th day of September 1937.

(Sgd.) Ewing Everett,
(Sgd.) O. H. Cherrillon,
Attorneys for Respondents on Review.

35 [Clerk's certificate to foregoing transcript omitted in printing.]

36 In United States Circuit Court of Appeals for the Second Circuit

No. 163—October Term, 1937

Argued Feb. 18, 1938. Decided March 7, 1938

Helvering, Commissioner of Internal Revenue, petitioner

v.

Donald H. Owens and Marion Haviland Owens, respondents

Appeal from the Board of Tax Appeals

Before L. Hand, Swan, and Chase, Circuit Judges

On petition to review an order of the Board of Tax Appeals expunging a deficiency in the respondents' income tax for 1934.

Louise Foster, of Washington, D. C., for petitioner.

Ewing Everett, of New York City, for respondents.

Opinion

Per curiam.

This appeal involves the question as to how much the taxpayers—a husband and wife filing a joint income tax return—were entitled to charge off as a loss for injury to a motorcar by reason of a collision in 1934. The car had been bought at some undisclosed time before 1934 for $1,825; on June 1st of that year it collided with another car and was so damaged that it was thereafter worth only $190; just before the collision it had been worth $225. The Commissioner allowed $35 as a loss—the difference between the value before the collision and after; the taxpayers claimed $1,635—the difference be-

tween the cost and the value after the collision. The Board ruled with the taxpayers.

Section 23 (e) (3) of the Revenue Act of 1934, 26 U. S. C. A. § 23 (e) (3)—following the language of earlier acts—provided that losses "of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck or other casualty," may be deducted; nobody disputes that collision is a "casualty." Subsection (h) of section 23, 26 U. S. C. A. § 23 (h), declared that "the basis for determining the amount of deduction for losses sustained, to be allowed under subsection (e) or (f), shall be the adjusted basis provided in section 113 (b)." Subsection (a) of section 113, 26 U. S. C. A. § 113 (a), declared that the "unadjusted basis" of property should be its cost; and subsection (b) (1) (B), section 113, 26 U. S. C. A. § 113 (b) (1) (B), that "exhaustion, wear and tear, obsolescence, amortization, and depletion" should be deducted from that "unadjusted basis" in cases when they were "allowed * * * under this Act." But section 23 (*l*), 26 U. S. C. A. § 23 (*l*) allowed for exhaustion, wear and tear, or obsolescence only in the case of "property used in the trade or business"; and on this account the respondents could not have claimed any deduction for wear and tear of the car during the years before 1934.

Verbally the conclusion is nevertheless inescapable that the "adjusted basis" was the same as the "unadjusted," and was the original cost; and, even though this secures to the owner a deduction which he could not have claimed, had he quite worn out the car without mishap, it may have been deliberately granted, for the destruction of property, still serviceable, often involves a greater loss to the owner than the money it would fetch on any market. Be that as it may, the letter is too plain; we should have to disregard the words,
and should not be interpreting them, if we refused to take them
37 just as they read. Colloquially, it is true, the whole loss was not "sustained" in 1934, as required by section 23 (e); but the earlier losses had never been "realized" in terms of money, and our income tax does not ordinarily "recognize" such losses; property used for convenience or pleasure, unlike business property, is no exception. The Treasury must take the bitter with the sweet; and just as increases in value do not increase the taxpayer's permissible deduction; (Pioneer Cooperage Co. v. Commissioner, 8 Cir., 53 F. 2d 43); so decreases should not decrease it.

Order affirmed.

38 In United States Circuit Court of Appeals, Second Circuit

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

DONALD H. OWENS AND MARION HAVILAND OWENS, RESPONDENTS

Judgment

Filed March 14, 1938

Appeal from the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be, and it hereby is, affirmed.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

WM. PARKIN, *Clerk.*

39 [File endorsement omitted.]

40 [Clerk's certificate to foregoing transcript omitted in printing.]

41 Supreme Court of the United States

Order allowing certiorari

Filed October 10, 1938

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] File No. 42665. U. S. Circuit Court of Appeals, Second Circuit. Term No. 180. Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Donald H. Owens and Marion Haviland Owens. Petition for a writ of certiorari and exhibit thereto. Filed July 6, 1938. Term No. 180 O. T. 1938.

U. S. GOVERNMENT PRINTING OFFICE, 1938

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In the Supreme Court of the United States

OCTOBER TERM, 1938

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

DONALD H. OWENS AND MARION HAVILAND OWENS

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above-entitled cause on March 14, 1938.

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 15–20) is unreported. The opinion of the Circuit Court of Appeals (R. 36–37) is reported in 95 F. (2d) 318.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered March 14, 1938 (R. 37–38). On mo-

tion of the petitioner, this Court entered an order on June 2, 1938, extending the time for filing a petition for writ of certiorari for 60 days from June 7, 1938 (R. 38). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the basis for determining the amount of a loss "sustained during the taxable year," through an accident to property which is not used in a trade or business and is not subject to an annual depreciation allowance, should be the original cost or the value immediately before the accident.

STATUTE INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * *

(e) *Losses by individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

* * * * * *

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. * * *

* * * * * *

(h) *Basis for determining loss.*—The basis for determining the amount of deduction for

losses sustained, to be allowed under subsection (e) or (f), shall be the adjusted basis provided in section 113 (b) for determining the loss from the sale or other disposition of property.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (unadjusted) of property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(b) *Adjusted basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) *General rule.*—Proper adjustment in respect of the property shall in all cases be made—

* * * * *

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws. * * *

STATEMENT

The Board, in adopting the stipulated facts, made substantially the following findings (R. 15–16):

The respondents are husband and wife. Prior to January 1, 1934, but after March 1, 1913, the

respondent Donald H. Owens purchased a Nash touring automobile at a cost to him of $1,825. The automobile at all times since has been, and was until June, 1934, used by him for his personal use only, and not in connection with any trade or business carried on by him. In June, 1934, by reason of an accidental collision with another automobile, the automobile was wrecked and partly demolished. It thereafter had a fair market value of $190. Immediately prior to such collision, the automobile had a fair market value of $225. He carried no insurance on the automobile and has not received any compensation through insurance or otherwise for any part of the loss sustained by reason of the accident. (R. 15–16.)

The respondent and his wife filed a joint income tax return for the calendar year 1934. No deduction on account of depreciation of the automobile was claimed or allowed during any taxable year. In the return for 1934 filed by the respondents, a loss deduction was claimed in the amount of $1,635, being the difference between the cost and the salvage value of the automobile immediately after the accident. The Commissioner allowed a deduction in the amount of $35, representing the difference between the fair market value of the automobile immediately prior to the accident and its salvage value immediately after the accident. (R. 16.)

The Board held that the deduction as claimed by the respondents should be allowed and determined

that there was no deficiency in tax for the year 1934 (R. 20-21).

The Circuit Court of Appeals affirmed the Board's decision (R. 37).

SPECIFICATION OF ERRORS TO BE URGED

1. The Circuit Court of Appeals erred in failing to hold that the amount of the deduction allowable to the respondents for the loss on their automobile which was used for personal purposes is the difference between the fair market value of the automobile immediately before the accident and its value thereafter, and in holding that the basis for determining the amount of the loss is the original cost.

2. The Circuit Court of Appeals erred in affirming the decision of the Board.

REASONS FOR GRANTING THE WRIT

The agreed value of the automobile immediately before the collision was $225 and, immediately afterwards, was $190. Thus the actual loss due to the collision was only $35. But the court below has approved a deduction of $1,635, the difference between the cost of the automobile and its value after the accident.

1. This decision seems contrary to well-established principles of tax law. The Revenue Acts have always restricted deductions for losses to those which were sustained during the taxable year, and Section 23 (e) (3), *supra*, itself permits de-

duction only for losses "sustained during the taxable year." It is plain that the loss which may be deducted under the decision of the court below was not sustained during the taxable year.

Moreover, under the stipulated facts the deduction of $1,635 represents a loss of only $35 due to the collision plus a further deduction of $1,600 due to accumulated depreciation and obsolescence. Section 23 (e) (3) permits deduction, as a loss arising from a casualty, of the former item, but there is no provision in the Revenue Act of 1934 permitting deduction for depreciation and obsolescence of property not used in a trade or business; much less is there a provision for deducting the accumulated depreciation or obsolescence of several preceding years.

In making a mechanical application of Section 23 (h), referring to Section 113, *supra*, the court below has lost sight of the basic structure of the Act. As this Court in *Helvering* v. *Morgan's, Inc.*, 293 U. S. 121, 126, has said that, "the true meaning of a single section of a statute in a setting as complex as that of the revenue acts, however precise its language, cannot be ascertained if it be considered apart from related sections, or if the mind be isolated from the history of the income tax legislation of which it is an integral part."

2. The decision of the court below is in direct conflict with the decision of the Circuit Court of Appeals for the Fourth Circuit in *Helvering* v.

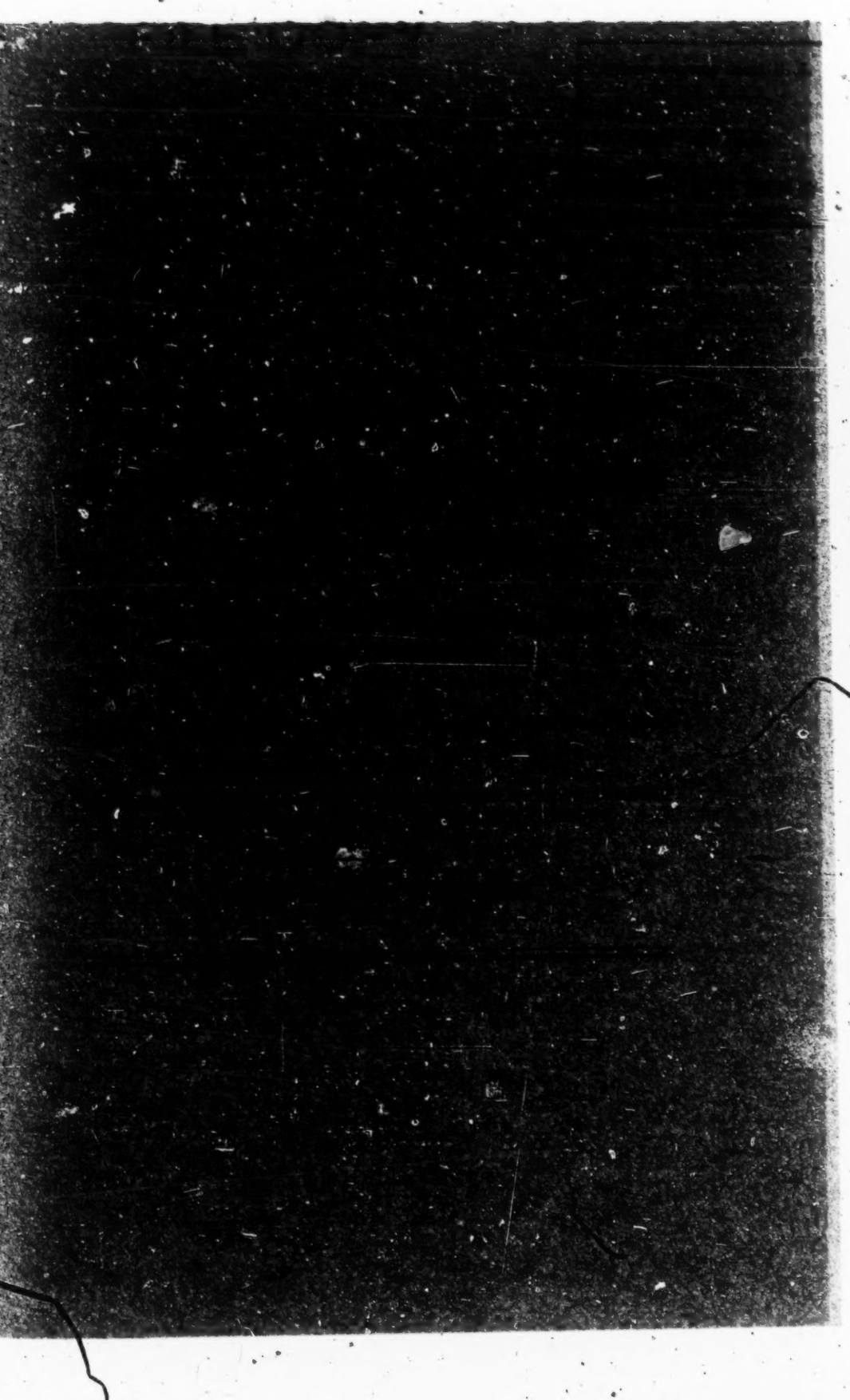
Obici, decided June 6, 1938, not yet reported but found in 1938 Prentice-Hall, Federal Tax Service, Vol. 1, par. 5.479. In that case the respondents in 1925 acquired a boat, boathouse, and pier at a cost of $5,325. The property was not used in a trade or business, and was totally destroyed by storm in 1933. The actual value of the property immediately prior to its destruction was $3,905. The Commissioner allowed the latter amount as a deduction. The Board of Tax Appeals ruled that the entire $5,325 must be allowed. The Circuit Court of Appeals reversed the Board. Speaking of the present decision of the court below, it said that "With due respect to the decision of the Second Circuit, we do not feel able to follow it." The Circuit Court of Appeals for the Fourth Circuit held that only the actual loss from the storm could be deducted because "The federal revenue laws have been consistent in allowing the deduction of only actual losses" and "only in the year sustained". It accordingly concluded that "it is hardly reasonable to suppose that Congress intended to allow a deduction as loss for the full cost of non-business property destroyed, notwithstanding such property had been depreciated through use."

Wherefore, it is respectfully submitted that this petition for a writ of certiorari should be granted.

ROBERT H. JACKSON,
Solicitor General.

JULY 1938.

U. S. GOVERNMENT PRINTING OFFICE: 1938



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In the Supreme Court of the United States

OCTOBER TERM, 1938

No. 180

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

DONALD H. OWENS AND MARION HAVILAND OWENS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 6–9) is unreported. The opinion of the Circuit Court of Appeals (R. 15) is reported in 95 F. (2d) 318.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered March 14, 1938 (R. 17). On June 2, 1938, the time within which a petition for a writ of certiorari could be filed was extended for a period

of sixty days from June 7, 1938 (R. 17). The petition for a writ of certiorari was filed on July 6, 1938, and was granted on October 10, 1938 (R. 17). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the basis for determining the amount of a loss "sustained during the taxable year," through an accident to property which is not used in a trade or business and is not subject to an annual depreciation allowance, should be the value immediately before the accident or the original cost.

STATUTES AND OTHER AUTHORITIES INVOLVED

The applicable portions of the pertinent statute and the other authorities involved will be found in the Appendix, *infra*, pp. 23–32.

STATEMENT

The Board of Tax Appeals, in adopting the stipulated facts, made substantially the following findings (R. 17):

The respondents are husband and wife. Prior to January 1, 1934, but after March 1, 1913, the respondent Donald H. Owens purchased an automobile at a cost to him of $1,825. The automobile at all times since has been, and was until June 1934, used by him for his personal use only, and not in connection with any trade or business carried

on by him. In June 1934, by reason of an accidental collision with another automobile, the automobile was wrecked and partly demolished. It thereafter had a fair market value of $190. Immediately prior to such collision, the automobile had a fair market value of $225. No insurance was carried on the automobile and no compensation through insurance or otherwise has been received for any part of the loss sustained by reason of the accident (R. 7).

The respondent and his wife filed a joint income tax return for the calendar year 1934. No deduction on account of depreciation of the automobile was claimed or allowed during any taxable year. In the return for 1934, filed by the respondents, a loss deduction was claimed in the amount of $1,635, being the difference between the cost and the salvage value of the automobile immediately after the accident. The Commissioner allowed a deduction in the amount of $35, representing the difference between the fair market value of the automobile immediately prior to the accident and its salvage value immediately after the accident (R. 7).

The Board held that the deduction, as claimed by the respondents, should be allowed and determined that there was no deficiency in respondents' income tax for the year 1934 (R. 9).

The Circuit Court of Appeals affirmed the Board's decision (R. 16).

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In failing to hold that the amount of the deduction allowable to the respondents for the loss of their automobile which was used for personal purposes is the difference between the fair market value of the automobile immediately before the accident and its value thereafter, and in holding that the basis for determining the amount of the loss is the original cost.

2. In affirming the decision of the Board.

SUMMARY OF ARGUMENT

The Government's position is that the loss deductible by reason of casualty is the amount of the loss resulting from the casualty; namely, the difference between the value of the automobile immediately before and that immediately after the collision. This position has been approved by the Circuit Court of Appeals for the Fourth Circuit in its recent decision in *Helvering* v. *Obici*, 97 F. (2d) 431, now pending on writ of certiorari in this Court, No. 318, present Term. The decision of the court below allowing a deduction of $1,635, measured by the difference between original cost and value after the collision, does violence to the provision of the Revenue Act of 1934 permitting a deduction under these circumstances and to settled provisions of the Revenue Acts.

Section 23 (e) (3) of the Revenue Act of 1934 allows the deduction of a loss sustained during the

taxable year if the loss arises from fires, storms, shipwreck, or other casualty. In the present case the loss from the casualty was $35, the additional $1,600 allowed by the court below representing the loss due to depreciation, the greater part of which occurred in previous years. The Revenue Acts have allowed deductions only for actual losses, and those only when sustained. An offset of losses sustained in other years against income of the taxable year is permissible only when specifically allowed. The decision below also grants a deduction for depreciation of non-business property which is denied by other provisions of the statute, and treats as the basis for determining the casualty loss the cost of property which was not the property suffering the damage. On the other hand, the use of value immediately prior to the collision resolves all of these inconsistencies.

The court below erroneously held that unadjusted cost must be used as the basis, on the ground that Section 23 (h) of the statute provides that the basis for losses shall be the adjusted basis prescribed in Section 113 (b), which in turn, in subdivision (1) B, provides that proper adjustment to cost shall in all cases be made for depreciation and other deductions, to the extent allowed (but not less than the amount allowable), and that since no such deductions are allowed or allowable in respect of non-business property, no adjustment of cost could be required in fixing the basis. Section 23 (h) necessitates the use of an adjusted basis, not cost, the un-

adjusted basis. Section 113 (b) is applicable to many other types of transactions in addition to casualty losses to non-business property, including gain or loss on the sale of property, losses incurred in trade or business, losses incurred in transactions entered into for profit, and corporate losses. Section 113 (b) (1) B will still have substantial application if, as we contend, the limitation on adjustments contained in that subdivision is construed to apply to situations where such adjustments represent allowable or allowed deductions, but not to apply where no such deductions are allowed, and in such case a reasonable adjustment for depreciation must be made. The use of value before the accident approximates cost less the reasonable adjustment for depreciation. If Section 113 (b) (1) B should nevertheless be deemed to apply in the case of non-business losses, it is limited by Section 23 (e) (3), and merely establishes a maximum beyond which the basis shall not rise, but not the minimum, where to so apply it would allow a deduction in excess of the loss from casualty, contrary to the legislative intent.

Prior decisions of this Court illustrate the principle that the basis provisions of the Revenue Acts are not inflexible and all-inclusive, but must be read in connection with the particular situation disclosed and the legislative intent as a whole. The regulations have never contained specific provisions with respect to non-business property as to which no

deductions for depreciation were allowed. The decisions and the administrative rulings have not been consistent and cannot be said to have prescribed a uniform rule. The final ruling of the Bureau of Internal Revenue, embodied in G. C. M. 16255, XV-1 Cumulative Bulletin 115, and the decision in the *Obici* case represent the reasonable and correct construction of the statute.

ARGUMENT

THE ONLY LOSS DEDUCTIBLE IS THAT ACTUALLY SUSTAINED DURING THE TAXABLE YEAR, WHICH IS CORRECTLY MEASURED BY THE DIFFERENCE BETWEEN THE VALUE OF THE AUTOMOBILE JUST BEFORE AND THE VALUE JUST AFTER THE ACCIDENT

The facts of this case can be simply stated. The respondent Donald H. Owens was the owner of an automobile, which had cost him $1,825. In June 1934 it had a value of $225. In that month it was damaged by a collision, as a result of which its value was decreased to $190. It is the Government's position that respondent is entitled to a deductible loss in the amount of $35, the difference between the value of the automobile just before and that just after the collision. This position has been approved in a similar case by the Circuit Court of Appeals for the Fourth Circuit. *Helvering* v. *Obici*, 97 F. (2d) 431, pending on writ of certiorari, No. 318, assigned for argument immediately following the present case. The respondent, on the other hand, claims a deductible

loss in the amount of $1,635, the difference between the original cost and the value after the collision. This position was approved by the Board and the court below.

The decision of the court below, we submit, does violence to the provision of the Revenue Act of 1934 permitting a deduction in these circumstances, and to settled principles embodied in all the Revenue Acts. Section 23 (e), *infra*, p. 23, allows as deductions "losses sustained during the taxable year and not compensated for by insurance or otherwise," including (paragraph 3) losses "of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft." The decision below has allowed as a deduction a loss which did not actually arise from casualty, and has allowed it in a year during which it was not sustained. The loss from casualty was a loss in value of $35. The additional $1,600 which respondent seeks to deduct represents a loss due to depreciation, a loss, moreover, which occurred not during the taxable year but over a previous period of years. It has been the settled policy of the Revenue Acts to allow as a deduction for losses only an actual loss, and to allow that only in the year when sustained. Cf. *United States* v. *White Dental Co.*, 274 U. S. 398; *Lucas* v. *American Code Co.*, 280 U. S. 445, 449; *U. S. Cartridge Co.* v. *United States*, 284 U. S. 511, 520; *Burnet* v. *Huff*, 288 U. S. 156; *Gowen* v. *Commissioner*, 65 F. (2d)

923, certiorari denied, 290 U. S. 687; *DeLoss* v. *Commissioner*, 28 F. (2d) 803 (C. C. A. 2d), certiorari denied, 279 U. S. 840; *Lewellyn* v. *Elec. Reduction Co.*, 275 U. S. 243. Income of one year cannot be offset by losses sustained in another year, except in those unusual situations where the statute specifically authorizes such an offset. *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, 363; *Burnet* v. *Thompson Oil & G. Co.*, 283 U. S. 301, 306; *Woolford Realty Co.* v. *Rose*, 286 U. S. 319, 326.

Furthermore, the decision below permits a deduction for depreciation in the case of non-business property although such a deduction is not allowed by the statute. The Revenue Act of 1934, Section 23 (l), *infra*, p. 24, permits as a deduction a reasonable allowance for the exhaustion, wear and tear of property "used in the trade or business." The regulations provide specifically that "The deduction of an allowance for depreciation is limited to property used in the taxpayer's trade or business. No such allowance may be made in respect of automobiles or other vehicles used solely for pleasure, * * *" Regulations 86, Article 23 (l)–2. And Section 24 (a) of the Act, *infra*, p. 24, provides that in computing net income no deduction shall in any case be allowed in respect of personal, living, or family expenses. The Revenue Acts have consistently refused the allowance of deductions for depreciation of property not used in the trade or business. See *F. M. Hubbell Son*

& Co. v *Burnet*, 51 F. (2d) 644 (C. C. A. 8th), certiorari denied, 284 U. S. 664. Deductions for depreciation are allowable only where specifically provided, and only in the years when sustained. *Burnet* v. *Thompson Oil & Gas Co.*, 283 U. S. 301, 306; *Kittredge* v. *Commissioner*, 88 F. (2d) 632 (C. C. A. 2d).

Finally, the decision below treats as the basis for determining the deductible loss the cost of property which was not the property suffering the damage by casualty. The property here involved is depreciable property. It was not the same just prior to the collision as it was at the time of purchase. This principle was concisely stated by the Court in *United States* v. *Ludey*, 274 U. S. 295, 301:

> When the plant is disposed of after years of use, the thing then sold is not the whole thing originally acquired. The amount of the depreciation must be deducted from the original cost of the whole in order to determine the cost of that disposed of in the final sale of properties. Any other construction would permit a double deduction for the loss of the same capital assets.

What was said in the *Ludey* case is applicable, *mutatis mutandis*, to the case at bar. The amount of depreciation of the automobile must be subtracted from the original cost in order to determine the cost of what has been subjected to loss. The construction adopted by the court below would permit a deduction for the loss of property by depreciation

where it has not been allowed by statute; would allow the unauthorized deduction in a year when that loss was not sustained; and would treat as the basis for determining loss the cost of property which was not the property suffering the damage by casualty.

A result so at odds with the basic principles of the Revenue Acts can be supported only if plainly compelled by the terms of the statute. Cf. *Mitchell v. Commissioner*, 48 F. (2d) 697, 700 (C. C. A. 2d), certiorari denied, 284 U. S. 646. The court below thought that the result was compelled by the provisions setting forth the basis to be used in determining gain or loss. Section 23 (h), *infra*, p. 23, provides that the basis for determining the amount of deduction for losses sustained shall be the adjusted basis provided in Section 113 (b) for determining the loss from the sale or other disposition of property. Section 113 (b), *infra*, p. 24, provides a so-called adjusted basis for determining gain or loss from the sale or other disposition of property. This basis is defined as cost adjusted, *inter alia*, for (paragraph B) "exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws * * *." The court below reasoned that since no exhaustion, wear and tear, or obsolescence was allowed or allowable in respect of non-business property under the statute, the ad-

justed basis in Section 113 (b), specifically made applicable to the facts of the present case by Section 23 (h), was in fact the same as the unadjusted basis provided in Section 113 (a), namely, the cost of the property damaged.

If the result thus reached by the court below were as plainly required by the terms of the basis provisions as the court felt it to be, the result would still be questionable because it fails to take into account other provisions of the statute, discussed above, which deny a deduction for depreciation in the case of non-business property, and which limit losses to those actually sustained in the taxable year. As was said in *Helvering* v. *Morgan's, Inc.*, 293 U. S. 121, 126:

> But the true meaning of a single section of a statute in a setting as complex as that of the revenue acts, however precise its language, cannot be ascertained if it be considered apart from related sections, or if the mind be isolated from the history of the income tax legislation of which it is an integral part.

A construction is to be avoided which will result in inconsistencies among the provisions of the Act. "Effect must be given to all the language employed, and inconsistent expressions are to be harmonized to reach the real intent of the legislature." *Iglehart* v. *Iglehart*, 204 U. S. 478, 485.

But it is submitted that the provisions setting forth the basis for determining gain or loss do not

require the result reached by the court below. It will be observed that Section 113 (a) refers to an "unadjusted" basis, namely cost, while Section 113 (b) prescribes the use of an "adjusted" basis. Obviously a significant distinction was intended between the two. The Revenue Act of 1932, Section 113 (b) (c. 209, 47 Stat. 169, 201) first provided for an *adjusted basis*. The provision was inserted in that form to clarify the rule which might not have been plain in all situations under previous Acts and to remove any doubts that upon the sale or other disposition of property the basis should be the net capital investment in the property at any point of time when it should become material to determine gain or loss, depreciation, or other deductions. See H. Rep. No. 708, 72d Cong., 1st Sess., pp. 18–19; S. Rep. No. 665, 72d Cong., 1st Sess., pp. 24–25. It is the provision for adjusted basis in Section 113 (b) which is made applicable by Section 23 (h) to losses of the character here involved. Yet the decision below makes applicable, in effect, the provision for unadjusted basis in Section 113 (a).

Moreover, the method by which the cost basis is to be adjusted, as provided in Section 113 (b) (1) (B), is not necessarily the method to be applied in the case of non-business property. The provision in question is applicable, it will be observed, to a large variety of losses, including losses to business property from casualty, losses in transactions en-

tered into by individuals for profit, and losses suffered by corporations. This is true because Section 23 (h) makes the adjusted basis applicable in determining deductions for losses sustained in all classes of cases under subsection (e) or subsection (f) of Section 23. Furthermore, it is applicable in all cases of gain or loss from the sale or other disposition of property. Consequently Section 113 (b) (1) (B) will have substantial scope if it is not literally applied to losses to non-business property. In this view the paragraph defines the measure of the adjustment for depreciation where the measure might be the amount allowed or the amount allowable; the paragraph makes clear which of these two is to be used. The paragraph does not constitute the authority for the adjustment; the authority is to be found in Section 23 (h) and Section 113 (b), which require that the basis shall be an "adjusted" basis. In the case of losses by casualty to non-business property, we suggest that the precise method of adjustment has not been provided, and that Section 23 (h) and Section 113 (b) read together merely require that the basis be cost reasonably adjusted. In this view the basis would be the value of the property at the time of the casualty, which approximates the depreciated cost of the property.

If Section 113 (b), (1) (B) is nevertheless deemed to govern the present case, it does not require the incongruous deduction allowed by the court below. In view of Section 23 (e) (3), confining deductible losses to those actually sustained,

the provisions of Section 113 (b) (1). (B) should be construed as establishing only a maximum figure beyond which the basis may not rise, but not establishing cost as a basis where to allow it would be to permit a loss in excess of that sustained and to allow a deduction elsewhere specifically denied. In other words, that paragraph requires that exhaustion, etc., be deducted from cost to the full extent allowed, or to the full extent allowable, whichever is greater; but it does not eliminate the necessity of subtracting depreciation in the case of non-business property where depreciation is neither allowed nor allowable under the Act. Nor does it require the use of cost of property other than that suffering the casualty.[1] Our interpretation prohibits the taxpayer from deducting as a loss more than the cost of his property, and does not permit him in all cases to deduct as much as the cost. If the actual loss is less than cost, he is limited to the amount of the actual loss as a deduction, where no previous deductions were allowable, in conformance with the legislative intent. This construction is that adopted by the Treasury Department. See G. C. M. 16255, XV–1 Cumulative Bulletin 115.

[1] So in *Heiner* v. *Tindle*, 276 U. S. 582, under a statute which required March 1, 1913, value as the basis, this Court adopted value as of 1901, which date marked the change from residential to commercial uses and accordingly brought the property for the first time within the purview of the deduction provisions of the Revenue Acts.

The use of value at the time of the casualty as a basis is in accord with the intent of the statute considered as a whole. It allows the deduction of the actual loss when sustained, it prohibits the deduction of losses suffered in other years, and it avoids the inconsistency of allowing deductions for losses which by another provision of the statute are specifically denied. Such a construction does no violence to the statutory language.

The decisions of this Court in analogous cases indicate the soundness of the Government's position. The provisions of the revenue acts which set forth the basis for determining gain or loss have on occasion been relied on as an inflexible and all-inclusive formula, without regard to the circumstances of the case and the other provisions of the act. Such a view of the basis provisions has been repeatedly rejected by this Court.

In *United States* v. *Flannery*, 268 U. S. 98, the taxpayer bought certain stock prior to March 1, 1913, and sold it in 1919 for more than its cost but for less than its value on March 1, 1913. The Revenue Act of 1918, which was applicable, provided that for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property the basis should be, in the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date. The taxpayer, resting his argument firmly upon the basis provisions, contended that he

was entitled to deduct a loss in the amount of the difference between the March 1, 1913, value and the sale price. This Court held, however, that the basis provisions were merely a limitation on the amount of gain or loss taxable or deductible, and that there must be an actual loss before the basis provisions for determining losses could be brought into play.

A similar problem was presented in *McCaughn v. Hollingsten*, 268 U. S. 106. In that case stock was bought prior to March 1, 1913, and was sold thereafter at a price which was less than either its original cost or the March 1, 1913, value. The March 1, 1913, value was, however, the higher figure, and the taxpayer sought to use it under the basis provisions of the Revenue Act of 1918, just described. In this case there was no question that an actual loss had been sustained, and it may have been supposed that the basis provisions must be literally applied as the taxpayer insisted. This Court held, however, that the case was governed by the decision in the *Flannery* case. The taxpayer was held entitled to deduct only his "actual loss," the difference between the purchase and selling prices, even though the Revenue Act prescribed the March 1, 1913, value as the basis.

United States v. *Ludey*, 274 U. S. 295, also indicates that the basis provisions must be construed in relation to other relevant provisions and to the underlying principles of the taxing Act. The Revenue Act of 1916, there involved, provided that the

basis for determining gain or loss on the sale of property acquired prior to March 1, 1913, should be its value as of that date, and no provision was made for adjusting the cost or March 1, 1913, value on account of depreciation or depletion. The taxpayer sold certain oil mining properties at less than original cost or the March 1, 1913, value. The taxpayer accordingly claimed a deductible loss. The Commissioner, however, insisted that the cost basis must be adjusted on account of depreciation and depletion, and that when such adjustment was made a gain on the sale was shown. This Court held that, despite the fact that the basis provisions did not provide for the deduction of depreciation and depletion from cost, such an adjustment must nevertheless be made. The Court stated (p. 300) that "Congress, in providing that the basis for determining gain or loss should be the cost or the 1913 value, was not attempting to provide an exclusive formula for the computation."

It is true that in the *Ludey* case the amount of depreciation and depletion required to be deducted from cost was not the full amount sustained but only that allowable by law as a deduction from gross income in past years. The reason given for adopting this measure was that Congress doubtless intended that the deduction to be made from original cost should be the aggregate amount which the taxpayer was entitled to deduct as a depreciation allowance (274 U. S. at 304). This aspect of the decision was further explained in *Burnet* v. *Thomp-*

case *Oil & Gas Co.*, 283 U. S. 301, 306-307, on the ground that an adjustment exceeding the amount allowable would tax more than the actual gain derived and have the effect of taxing in part a return of capital. Neither of these considerations is applicable in the case at bar. Here it is clear from other provisions of this and prior Acts that Congress intended to allow no deduction for depreciation; and the question whether more than actual gain is taxed has no bearing, since we are dealing not with a gain but with a deductible loss, a matter of legislative grace.

The foregoing decisions go far to suggest the sound result in the present case. They warn against a reading of the basis provisions as an all-inclusive formula for determining losses, and they are a reminder that those provisions are designed to implement the controlling provisions which permit deductions only for losses actually sustained, arising from the events enumerated, and suffered in the taxable year.

With respect to the precise issue here presented, the decisions and the administrative rulings as well have not been consistent, and accordingly cannot be said to have prescribed a uniform rule. In some cases a basis other than cost was used;[2] in others

[2] *Webb* v. *Commissioner*, 1 B. T. A. 759; *Shearer* v. *Anderson*, 16 F. (2d) 995 (C. C. A. 2d) [deductible loss measured by the cost of repairs]; *Buckwalter* v. *Commissioner*, 20 B. T. A. 1005, affirmed on other points, 61 F. (2d) 971 (C. C. A. 6th) [difference between the value at the time of

cost was adopted.[1] The Board of Tax Appeals has followed the latter view in the present case and in *Helvering* v. *Obici*, *supra*.

The regulations have never contained specific provision with respect to non-business property as to which no deductions for depreciation were allowable. Article 141, Regulations 45, promulgated under the Revenue Act of 1918, provided generally as to casualty losses that the basis should be cost adjusted by the amount which had been or should have been set aside and deducted in the current year and previous years from gross income on account of depreciation. Article 141, Regulations 62, promulgated under the Revenue Act of 1921, provided that the deduction for casualty loss should be the difference between the cost of the property, less proper adjustments for depreciation, and the salvage value. Article 141, Regulations 65, promulgated under the Revenue Act of 1924, provided generally as to all losses that the basis should be the same as that for gain or loss upon sale, with

---

the casualty and the salvage value]. Cf. *Grant* v. *Commissioner*, 30 B. T. A. 1028, where an arithmetical formula based upon cost and value prior to and after the casualty was used.

[1] *Brooks* v. *Commissioner*, 12 B. T. A. 31, affirmed on other grounds, 35 F. (2d) 178 (C. C. A. 4th); *O'Rear* v. *Commissioner*, 28 B. T. A. 698, 701, overruling *Buckwalter* v. *Commissioner*, *supra*, affirmed on this point in *O'Rear* v. *Commissioner*, 80 F. (2d) 473 (C. C. A. 6th), on the ground that the question was not properly raised before the Board of Tax Appeals. Cf. *Bass* v. *Commissioner*, 30 B. T. A. 4.

proper adjustment for items of loss, depreciation, obsolescence, amortization or depletion previously allowed with respect to the property. Article 141, Regulations 69, promulgated under the Revenue Act of 1926, provided that the basis for losses should be the same as that for gain or loss upon sale, with proper adjustment for depreciation, obsolescence, amortization or depletion, the proper adjustment being defined by reference to Article 1561 as the amount which had been allowed since the acquisition of the property, whether or not such deductions were claimed by the taxpayer or formally allowed. Similar provisions are contained in Article 171 of Regulations 74 and 77, promulgated under the Revenue Acts of 1928 and 1932, respectively, and Article 23 (h)–1 of Regulations 86 and 94, promulgated under the Revenue Acts of 1934 and 1936, respectively.

The administrative rulings have varied. I. T. 1567, II–1 Cumulative Bulletin 90, did not specifically rule on the subject, holding merely that a claimed loss through depreciation of land due to the action of the sea was merely conjectural and indeterminate and could not be deducted as a casualty loss. I. T. 2217, IV–2 Cumulative Bulletin 53, ruled that upon the destruction of a residence by fire undepreciated cost formed the basis for the deductible loss, since the taxpayer had not been permitted to deduct depreciation in prior years. This ruling was followed in I. T. 2231, IV–2 Cumulative Bulletin 53. These rulings were disapproved by

G. C. M. 16255, XV–1 Cumulative Bulletin 115, holding that the deductible loss from casualty to non-business property is the difference between the value immediately before and immediately after the casualty, and I. T. 2217 and I. T. 2231 were modified accordingly by I. T. 2966, XV–1 Cumulative Bulletin 299. This is the present position of the Treasury Department.

For the reasons advanced heretofore, we submit that the final ruling of the Commissioner in G. C. M. 16255, *supra*, and the decision of the Circuit Court of Appeals for the Fourth Circuit in *Helvering* v. *Obici*, *supra*, represent the reasonable and correct construction of the statute.

CONCLUSION

The decision of the Circuit Court of Appeals is erroneous and should be reversed.

Respectfully submitted.

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NOVEMBER 1938.

APPENDIX

STATUTE AND OTHER AUTHORITIES INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 690:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft.

* * * *

(f) *Losses by corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * *

(h) *Basis for determining loss.*—The basis for determining the amount of deduction for losses sustained, to be allowed under subsection (e) or (f), shall be the adjusted basis provided in section 113 (b) for determining the loss from the sale or other disposition of property.

* * * * *

(l) *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. * * * [U. S. C., Title 26, Sec. 23.]

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses;

* * * * * *

[U. S. C., Title 26, Sec. 24.]

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) * * * [U. S. C., Title 26, Sec. 41.]

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (unadjusted) of property.*—The basis of property shall be the cost of such property; except that—

* * * * * *

(b) *Adjusted basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) *General rule.*—Proper adjustment in respect of the property shall in all cases be made—

* * * * * *

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the

amount allowable) under this Act or prior income tax laws. * * * [U. S. C., Title 26, Sec. 113.]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 23 (e)—1. *Losses by individuals.*—Losses sustained by individual citizens or residents of the United States and not compensated for by insurance or otherwise are fully deductible if (*a*) incurred in the taxpayer's trade or business, or (*b*) incurred in any transaction entered into for profit, or (*c*) arising from fires, storms, shipwreck, or other casualty, or theft, and a deduction therefor has not prior to the filing of the return been claimed for estate tax purposes in the estate tax return, or (*d*) if not prohibited or limited by any of the following sections of the Act: Section 23 (g), relating to wagering losses; section 24 (a) (6), relating to losses from sales or exchanges of property between members of a family or between a corporation and its shareholders; * * *

In general losses for which an amount may be deducted from gross income must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed. Substance and not mere form will govern in determining deductible losses. Full consideration must be given to any salvage value and to any insurance or other compensation received in determining the amount of losses actually sustained. (See section 113 (b).)

A loss occasioned by damage to an automobile maintained for pleasure, where such damage results from the faulty driving of

the taxpayer or other person operating the automobile, but is not due to the willful act or willful negligence of the taxpayer, is a deductible loss in the computation of net income. If damage to a taxpayer's automobile results from the faulty driving of the operator of an automobile with which the automobile of the taxpayer collides, the loss occasioned to the taxpayer by such damage is likewise deductible. No loss is realized by the transfer of property by gift or by death. But see section 44 (d).

A loss on the sale of residential property purchased or constructed by the taxpayer for use as his personal residence and so used by him up to the time of the sale is not deductible. * * *

ART. 23 (b)-1. *Basis for determining loss.*—The basis for determining the amount of the deduction for losses is the same as is provided in section 113 for determining the loss from the sale or other disposition of property. Proper adjustment must be made in each case for any expenditure, receipt, loss, or other item properly chargeable to capital account, and for depreciation, obsolescence, amortization, or depletion. (See section 113 (b).)

ART. 113 (b)-1. *Adjusted basis: General rule.*—* * *

* * * * * *

The cost or other basis must also be decreased by the amount of the deductions for exhaustion, wear and tear, obsolescence, amortization, and depletion to the extent such deductions have in respect of any period since February 28, 1913, been allowed (but such decrease shall not be less than the amount of deductions allowable) under the Revenue Act of 1934 or prior income tax

laws. The adjustment required for any taxable year or period is the amount allowed or the amount allowable for such year or period under the law applicable thereto, whichever is the greater amount. A taxpayer is not permitted to take advantage in a later year of his prior failure to take any depreciation allowance or of his action in taking an allowance plainly inadequate under the known facts in prior years. The determination of the amount properly allowable shall, however, be made on the basis of facts reasonably known to exist at the end of such year or period. The aggregate sum of the greater of such annual amounts is the amount by which the cost or other basis of the property shall be adjusted. * * *

G. C. M. 16265, XV-1 Cumulative Bulletin 115-118:

SECTION 23 (e).—DEDUCTIONS FROM GROSS INCOME: LOSSES BY INDIVIDUALS.

ARTICLE 23 (e)-1: Losses by individuals.

REVENUE ACT OF 1934

* * * * *

Advice is requested relative to the determination of the amount of the loss deductible under the provisions of section 23 (e) 3 of the Revenue Act of 1934 where an automobile purchased for the taxpayer's personal use was damaged in a collision.

In the year 1929 the taxpayer purchased an automobile for his personal use at a cost of 7x dollars. In the year 1934 he had a collision, not due to his own recklessness, at which time he carried no collision insurance. Just prior to the collision the automobile had been appraised for trade-in purposes at 3.60x dollars. After the collision the car

was limited to but the allowance was only [illegible] dollars.

Section 23 (e) 2 of the Revenue Act of 1934 provides that in computing the taxable net income of an individual there shall be allowed as a deduction losses sustained during the taxable year and not compensated for by insurance or otherwise of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. In interpreting the corresponding section of prior Revenue Acts, it has been held that a loss resulting from an automobile collision, where such accident was not due to the wilful act or wilful negligence of the taxpayer, is deductible as a loss arising from "other casualty" (*Shearer v. Anderson*, 10 Fed. (2d), 965; *W. S. Brunson v. Commissioner*, 2 B. T. A. 1008, acquiescence, C. B. VIII-1, 6; *Tracy V. Batchelder v. Commissioner*, 20 B. T. A., 1005; I. T. 2408, C. B. VI-1, 85; and article 23 (e)-1 of Regulations 86).

Section 23 (h) of the Revenue Act of 1934 provides that the basis for determining the amount of deduction for losses sustained, to be allowed under section 23 (e) of that Act, shall be the adjusted basis provided in section 113 (b) for determining the loss from the sale or other disposition of property. Under the provisions of section 113 (b) of the Revenue Act of 1934, the basis for determining gain or loss from the sale or other disposition of property acquired after February 28, 1913, with certain exceptions inapplicable in the instant case, is the cost of such property, diminished as provided by section 113 (b) 1 (B) for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less

than the amount allowable) under that Act or prior income tax laws.

In *Tracy F. Buchwalter* v. *Commissioner*, supra, the Board of Tax Appeals allowed as a deduction in the case of an automobile damaged by fire in 1927 only the difference between the actual value immediately prior to the fire and the salvage value.

In *Heiner* v. *Tindle* (276 U. S. 582), arising under the Revenue Act of 1918, the taxpayer built a residence in 1888, used it as a residence until 1901, and leased it beginning in 1901 until he sold it in 1920. The United States Supreme Court held that there occurred in 1901 a transaction entered into for profit, and since the fair market value of the property on March 1, 1913, was less than the value in 1901, and less than actual cost, the taxpayer sustained a deductible loss of the difference between the March 1, 1913, value and the selling price.

In *Mitchell* v. *Commissioner* (48 Fed. (2d), 697, certiorari denied, 284 U. S., 646), the Circuit Court of Appeals for the Second Circuit said in a case arising under the Revenue Act of 1921—

> The allowance of anything beyond an actual loss would be most unlikely in the absence of a clear legislative mandate. The provision in section 214 (a) (6) that losses are to be computed upon the basis of the "fair market price or value as of March 1, 1913," should be construed, like other similar clauses, as merely a limitation upon losses that would otherwise have been deductible. While Congress can, of course, allow such deductions as it pleases and limit them as it will, it can not reasonably be thought to have intended in any case to have allowed more than actual losses * * *.

In *George DeBeck v. Commissioner* (23 B. T. A., 710, acquiescence, C. B. XI-1, 2), the Board said:

> The Treible decision in effect holds that in determining the loss sustained from the sale of property originally acquired as a residence and later converted into business property, the rule is to compute the amount of the loss, first, in accordance with the applicable statute dealing with the computation of gain or loss from the sale or other disposition of property, and, second, to allow as a deduction only that portion of the loss so determined as occurred subsequent to the time the property was converted into business use.
>
> * * * * * *
>
> It is our opinion that the instant case is controlled by section 204 (b), supra, and that the value in 1916 should be used only as a limitation upon the actual loss prescribed by the statute. * * *

In *Charles J. Thatcher v. Commissioner* (24 B. T. A. 1130) the Board said:

> * * * When residential property is converted into business property, it is the fair market value of the property at the time of conversion which represents the cost of the business property. * * *

The above reasoning has been carried into article 23 (e)-1 of Regulations 86 in interpreting section 23 (e) of the Revenue Act of 1934. That article provides in part as follows:

> *Losses by individuals.*—* * *
>
> * * * * * *
>
> * * * If, however, property so purchased or constructed is prior to its sale rented or otherwise appropriated to income-producing purposes and is used for such

purposes up to the time of the sale, a loss from the sale of the property, computed as provided in section 111, is, subject to the limitations provided in section 117, an allowable deduction in an amount not to exceed the excess of the cost or other basis of the property at the time it was appropriated to income-producing purposes (with proper adjustment for depreciation) over the amount realized from the sale. [Italics supplied.]

The example set forth in article 23 (e)-1 shows clearly a computation wherein the allowable loss is limited to the actual loss sustained, based upon the value of the property when converted to income-producing purposes, although the provisions of section 23 (h) are equally applicable.

Section 23 (e) 3 of the Revenue Act of 1934 allows as a deduction certain losses sustained during the taxable year, including losses arising from "other casualty." Such losses must be *actually sustained*. In such a case it is not the purchase price of the property which is lost but the value of the property at the time of the casualty. It is the opinion of this office that the provisions of section 23 (e) 3 are controlling with regard to the deductibility of such losses by individuals, and that such losses are limited thereby to the amount of loss *actually sustained*; and that section 23 (h) which provides that a loss must be determined or measured by the adjusted basis is a limitation provision. Therefore, although computation must be made in accordance with section 23 (h) and section 113, the amount deductible is the loss *actually sustained*, and not in excess of the amount computed under section 113. As stated above, this view was adopted

in Regulations 65 and is clearly set forth in the example relating to loss from sale of property purchased as a residence but later converted to income-producing purposes.

In the present case the taxpayer's automobile was valued just prior to the collision at [illegible]x dollars. Just after the collision its value was only 1,07x dollars. The loss actually sustained as a result of the collision was, therefore, the difference between those amounts, or 2,53x dollars. Since that amount is not in excess of the amount computed under section 118, it follows that 2,53x dollars is the amount of the loss allowable as a deduction under section 23 (e) 3.

In view of the fact that the position adopted herein is not in accord with the conclusion reached in I. T. 2217 (C. B. IV–2, 53) that upon the destruction of a residence by fire in the year 1924 the deductible loss sustained was the difference between the cost of the property (without any adjustment for depreciation) and the insurance or other compensation received, reduced by the salvage value, if any, of the property, or with the conclusion reached in I. T. 2231 (C. B. IV–2, 53) that the amount of a loss sustained by a taxpayer through the bursting of a boiler used in the heating of his residence is the difference between the basis of the boiler and the insurance or other compensation received, reduced by the salvage value of the boiler, if any, it is recommended that I. T. 2217 and I. T. 2231 be modified accordingly.

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IN THE

Supreme Court of the United States,

October Term—1933.

No. 180.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

vs.

DONALD H. OWENS and MARION HAVILAND OWENS,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENTS.

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In the

Supreme Court of the United States.

October Term, 1938.

Guy T. Helvering, Commissioner of Internal Revenue,
Petitioner,

vs.

Donald H. Owens and Marion Haviland Owens,
Respondents.

No. 180.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF FOR RESPONDENTS.

Opinions of the Courts Below.

The memorandum opinion of The Board of Tax Appeals (R. 6-9) is unreported. The opinion of the Circuit Court of Appeals (R. 15-16) is reported in 95 F. (2d) 318.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered March 14, 1938 (R. 17). On motion of the petitioner, this Court entered an order on June 2, 1938, extending the time for filing a petition for writ of certiorari for sixty days from June 7, 1938. A petition for a writ of certiorari was filed July 6, 1938 and was granted October 10, 1938 (R. 17). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

Question Presented.

Whether, for Federal Income Tax purposes, the amount of the deduction allowable upon the destruction of a pleasure automobile, where only a salvage value remains, is measured by the difference between the cost of the car and the salvage value thereof, or is limited to the difference between the value of the car before the accident and its salvage value.

Statement of Facts.

The facts have been correctly summarized in the statement of facts made at pages 2-3 of the petitioner's brief.

Statutes Involved.

Revenue Act of 1934, c. 277, 48 Stat. 680.

"Section 23.—Deductions From Gross Income:

In computing net income there shall be allowed as deductions:

* * * * * * *

(e) Losses by Individuals.—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. No loss shall be allowed as a deduction under this paragraph if at the time of the filing of the return such loss has been claimed as a deduction for estate tax purposes in the estate tax return.

* * * * * * *

(h) Basis for Determining Loss.—The basis for determining the amount of deduction for losses sus-

tained, to be allowed under subsection (e) or (f), shall be the adjusted basis provided in section 113(b) for determining the loss from the sale or other disposition of property."

"Section 113.—ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) BASIS (UNADJUSTED) OF PROPERTY.—The basis of property shall be the cost of such property; except that—

* * * * * * *

(b) ADJUSTED BASIS.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) GENERAL RULE.—Proper adjustment in respect of the property shall in all cases be made—

* * * * * * *

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws. * * *"

(C) in respect of any period prior to March 1, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent sustained;

* * * * * * *

Summary of Argument.

The issue of law presented herein is identical with that presented in the case of *Amedeo Obici and Mrs. Amedeo Obici (Husband and Wife)* v. *Guy T. Helvering, Commissioner of Internal Revenue* now pending here (October Term, 1938, Number 318) on writ of certiorari granted to the United States Circuit Court of Appeals for the Fourth Circuit, in which case the taxpayers are the petitioners to this Court. The *Obici* case has been placed upon the calendar of

this Court for argument immediately following the case herein (Number 180). The arguments advanced in petitioners' brief in Number 318 are of equal applicability to the issue presented herein (Number 180) and are adopted and incorporated herein by reference.[1]

In the *Obici* case (No. 318) the taxpayers' boat, boathouse and pier, not used in a trade or business, were totally destroyed by storm. In the case herein presented the respondents' pleasure car was destroyed by an accident so that only a salvage value remained. The existence of a salvage value does not render different principles applicable to the case presented herein. Where such salvage value remains, it is simply to be subtracted from the "basis" in determining the amount of deductible loss. Regulations 86, Article 23(e)-1 provides in part as follows:

> * * * "Full consideration must be given to any salvage value and to any insurance or other compensation received in determining the amount of losses actually sustained. See section 113(b)."

Article 23(e)-3 of Regulations 86 also provides that in determining the amount of the deduction where loss of useful value is sustained on business property the amount of the deduction is the difference between the prescribed "basis" and "the salvage value of the property".

In the instant case the Board of Tax Appeals found that respondents' automobile was wrecked and partly demolished

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[1] The *Obici* case (Number 318) is governed by the Revenue Act of 1932. The case herein (Number 180) is governed by the Revenue Act of 1934. The provisions of the two Acts, insofar as material to the issue presented, are in all respects alike. Section 23(e)(1), (2) and (3) and Section 23(f) of each Act governs property losses. The "basis" section for determining the amount of the loss allowable under Section 23(e) in the Revenue Act of 1932 is numbered Section 23(g); in the Revenue Act of 1934 it is numbered Section 23(h). In applying petitioners' brief in Number 318 to this case "Section 23(g)" should be read as "Section 23(h)," the equivalent section in the Revenue Act of 1934. The pertinent provisions of Section 113(a) and (b) in the Revenue Act of 1932 and the Revenue Act of 1934 are identical.

so that only a salvage value remained (R. 8). In the opinion of the Board of Tax Appeals, the Board stated:

> "It is apparent from the stipulation of the parties, to the effect that the automobile was wrecked and partly demolished so that a salvage value only remained, that a complete loss resulted except for the value of the salvage remaining after the collision" (R. 8).

In cases involving slight damage where the property can be repaired at a relatively small expense, retains its useful value, and continues to be used by the taxpayers for the purposes for which it was acquired, then the loss deduction is determined by some other measure independent of cost, such as the cost of repairs. The facts here, however, indicate a loss of useful value and the existence of only a salvage value after the wreck.

The fact that the salvage value here was not greatly below the value of the car before the wreck is due to the fact that a car which is completely wrecked has a high "trade-in" value as an inducement to buy a new car.

Where the property is "partly demolished" so that for practical purposes all *useful* value is lost and only a junk or salvage value remains respondents submit that under Section 23(h) and Section 113 (b) the proper measure for computing the deductible loss is cost, less salvage value.

ARGUMENT.

I.

Petitioner's argument that the Circuit Court below erred in permitting an unauthorized deduction for depreciation in the case of nonbusiness property, is not within the scope of petitioner's specification of errors.

The crux of petitioner's argument is that the decision below, by reason of the employment of cost as a "basis", permits indirectly the deduction of depreciation sustained in prior years on property not used in a trade or business, where the statute does not permit a deduction for physical wear and tear as such. Petitioner even argues that "the amount of depreciation of the automobile must be subtracted from the original cost in order to determine the amount of what has been subjected to loss."[1] Petitioner's brief, page 10.

Petitioner, in his specification of errors to be argued before this Court, alleges only that the Circuit Court of Appeals erred in failing to hold that the amount of the deduction allowable to respondents is the difference between the fair market value of the automobile immediately before the accident and its value thereafter. (Petition for the Writ of Certiorari, p. 5; Petr.'s Br., p. 4.) Petitioner now apparently contends as well that the Court below erred in failing to hold that cost less "the amount of depreciation of the automobile" was the proper basis. Petitioner's brief, page 10. Such a contention does not come within the scope of petitioner's allegations of error.

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[1] This same argument was advanced by the Government in *United States* v. *Ludey*, 274 U. S. 295, and was rejected by this Court which then held that the cost under the 1916 Act should be reduced by the amount of depreciation and depletion which "the taxpayer was entitled to deduct in the several years" prior to the year of sale.

Cost less depreciation is not necessarily the same as fair value before the casualty. A suit of clothes or a personal automobile when purchased and converted to personal uses for even a short while, decreases in value owing to other factors at a far greater rate than the rate of actual physical depreciation. On the other hand a residence while physically depreciating may at the same time actually increase in value. It is submitted that petitioner's specification of errors does not include within its scope an allegation that the Circuit Court erred in not subtracting physical depreciation from cost in determining the proper basis for computing the amount of the deductible loss. If the specifications are broad enough to permit such an allegation it should be denied as unsound. *United States* vs. *Ludey*, 274 U. S. 295.

2.

There are numerous instances in the revenue acts and the cases thereunder permitting the use of a "basis" under the "basis sections" which indirectly gives the taxpayer the benefit of unallowable depreciation physically sustained in prior years.

Petitioner argues that the use of cost as a basis permits the taxpayer to receive the benefit of depreciation deductions which were unallowable and unauthorized in prior years and that for this reason a special limitation should be found in the words "losses sustained during the taxable year" in Section 23(e). (Petr.'s Br., pp. 9, 10, 11.)

There are numerous instances in the Revenue laws where the basis authorized, and the loss computed thereunder, may indirectly include as part of the loss allowed, physical depreciation sustained in prior years and unauthorized as a deduction by any of the Revenue Acts. The Revenue Act of 1924, is the most striking example. Section 214(a)(4) of

that Act provided that in computing net income there should be allowed as a deduction "losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business". Under Section 204(a) the basis prescribed for determining gain or loss was cost. Section 202(a) provided that the deductible loss should be the excess of "such basis" (cost) over the amount realized. Section 202(b) provided—

> "In computing the amount of gain or loss under subdivision (a) proper adjustment shall be made for (1) any expenditure properly chargeable to capital account, and (2) any items of loss, exhaustion, wear and tear, obsolescence, amortization, or depletion, *previously allowed* with respect to such property." [1] (Italics supplied.)

Under these Sections the question arose whether (1) an adjustment should be made under Section 202(b) for depreciation sustained on the property for years prior to the income tax laws and (2) whether adjustment should be made for the excess of depreciation actually physically sustained over that *actually allowed* by the Commissioner as deductions in previous years.

The Board of Tax Appeals, the Courts, and the Treasury Department itself failed to find that the words "losses sustained during the taxable year" contained in Section 214(a)(4) of the Revenue Act of 1924 required an interpretation of Section 202(b) of that Act such as would disregard and circumvent the literal meaning of that Section. The General Counsel's Office of the Bureau of Internal Revenue at first ruled that the "basis" was required to be reduced by Section 202(b)(2) of the Revenue Act of 1924 "only for deductions (depreciation) which have in prior years been actually granted by the Commissioner in computing the net income of the taxpayer," and that it was not required that the "basis"

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[1] The adjustment required under the 1934 Act is for depreciation "allowed" or "allowable," whichever is greater.

be reduced by the amount of physical depreciation actually sustained before 1909. *G.C.M. 8573*, Cumulative Bulletin IX—2, page 168. See also *S.M. 4249*, Cumulative Bulletin IV—2, page 15.

The Board of Tax Appeals in *Ann Arbor Railroad Co. v. Commissioner*, 29 B.T.A. 331, held that the "basis" should be reduced by depreciation actually and physically sustained on the property prior to 1909. Accordingly, the General Counsel's Office revoked *G.C.M. 8573* (*supra*) and *S.M. 4249* (*supra*) in *G.C.M. 10754*, Cumulative Bulletin XI—2, page 177. However, the Board of Tax Appeals in *Union Pacific Railroad Co. v. Commissioner*, 32 B.T.A. 383, reversed its former decision in the *Ann Arbor Railroad* case (*supra*) and held that the "basis" should not be reduced for depreciation actually sustained but not allowed (before 1909). The Board was affirmed by the Second Circuit in 86 F. (2d) 637. The same conclusion was reached in *Helvering v. St. Louis Southwestern Railway Co.*, 84 F. (2d) 857. In view of these cases the General Counsel in *G.C.M. 18611*, Cumulative Bulletin 1937—1, page 235, revoked *G.C.M. 10754* (*supra*) and reinstated *G.C.M. 8573* (*supra*).

In the *Union Pacific Railroad Co.* case (*supra*) the reasons of the Board were set forth in the opinion (pp. 395-397) as follows:

> "For any year prior to 1924, the determination of gain or loss upon the sale or disposition of depreciable property was governed by a statute which made no mention of an adjustment for prior depreciation. Whether depreciation should be taken into account in the computation and, if so, whether the measure of such depreciation should be the amount "sustained", or the amount accounted for on the books, or the amount deducted on the returns, was a question upon which there was no consensus. The Revenue Act of 1924 was a deliberate attempt by Congress to set the question at rest. The Treasury sought legislative sanction for its regulation and practice of deducting original cost by depreciation regarded as actually sustained. Regulations 45, art. 1561, or sustained and allowable, Regulations 62, art.

1561, irrespective of the extent to which such depreciation had been actually used as a factor of tax computation. This, however, the Congress failed to adopt. It provided for an adjustment for prior depreciation, but expressly limited such adjustment to the depreciation "previously allowed". Cost was left undistributed in arriving at the basis, section 204, and the adjustment was povided for in the computation of gain or loss in section 202.

We can find no justification for the view, urged by respondent, that the term "cost", used in section 204, means depreciated cost or cost less depreciation. Since provision was explicitly made in section 202 for the depreciation adjustment in computing gain or loss, there is no ground for an inference that a similar adjustment is, by implication, to be imported into section 204. This would result in the same sort of illogical computation as the Government was seeking, by the new statute, to prevent.

That there was reason for Congress to limit the adjustment to so much as had inured to the taxpayer's tax benefit and to disregard the depreciation which had had no tax effect, is apparent from United States v. Ludey, supra, in which the Supreme Court reasoned to a similar conclusion under the earlier acts.

The respondent sets forth supposititious cases to demonstrate what he regards as the absurd effect of disregarding actual depreciation of earlier years. These illustrations are, however, so common-place that it is difficult to believe that they escaped legislative consideration. On the other hand, there is more to be said for the view that Congress recognized the diverse views and practices which had marked the history of depreciation, and sought to adopt a simple computation which would avoid the difficulties which the concept of sustained depreciation would entail' " * * *. (Italics supplied.)

See also *United States* v. *Ludey, supra*, where this Court held under the 1916 Act that cost should not be reduced by depreciation "sustained" but only by the aggregate of the depreciation which was *deductible* under the income tax laws.

3.

In the computation of gain as well as in the computation of losses Congress has enacted specific ameliorating provisions for taxpayers who have been deprived of the useful value of their property through fire, storm, shipwreck, or other casualty, or theft.

In *Amedeo Obici and Mrs. Amedio Obici* v. *Helvering*, No. 318, the Fourth Circuit suggested that unintended error crept in when the casualty loss provisions were drawn and intimated that Congress intended no special "tax benefits" in the case of casualty loss.

On the contrary, Congress has definitely shown a desire to accord special consideration to those taxpayers who are involuntarily deprived of the use of their property. This extends even to those cases where a profit (from insurance for example) may have resulted. Section 112(f) of the Revenue Act of 1934 provides as follows:

> "(f) INVOLUNTARY CONVERSIONS.—*If property (as a result of its destruction* in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) *is* compulsorily or *involuntarily converted into* property similar or related in service or use to the property so converted, or into *money* which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, *no gain* or loss *shall be recognized*. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended." (Italics supplied).

Section 112(f) or substantially similar Sections has been in the law since the Revenue Act of 1921, where it first appeared as Section 214(a)(12). The legislative history of the Revenue Act of 1921 reveals a legislative intent to confer ameliorating benefits upon the taxpaper who is deprived of his property by a sudden force over which he has no control. Thus, the Report of the House Ways and Means Committee on the Revenue Act of 1921, 67th Congress, First Sessions, H. R. Report No. 350, page 12, provides:—

> "Section 217 (Section 214(a)(13) in the final draft) deals with cases where property is involuntarily converted into cash as a result of fire, shipwreck, condemnation, or related causes; and permits the taxpayer to omit or deduct the gains involuntarily realized, when he proceeds forthwith in good faith to invest the proceeds of such conversion in the acquisition of similar property or in the establishment of a replacement fund therefor." (Parentheses supplied.)

4.

The rule applicable to adjustments for depreciation on business properties set forth by this court in *United States* vs. *Lesley* is equally applicable to non-business "casualty" losses and supports respondents' contentions.

The case of *United States* vs. *Lesley*, (*supra*) involved the computation of gain or loss on a sale of business property in 1917. The Revenue Act of 1916 which governed the transaction made no specific provisions for adjustments on account of depreciation in determining the gain or loss. The Government argued that all depreciation previously actually *sustained* on the property should be deducted from cost in computing the "basis" and that "for this reason, the cost to plaintiff of the net property sold in 1917 was not $95,977.33 but $53,258.36". The taxpayer contended that cost was the

proper basis because the Revenue Act contained no provisions with respect to adjustments for depreciation. This Court rejected the contentions of both the taxpayer and the Government, Justice Brandeis stating in the course of the opinion—

> "* * * On the other hand, we cannot accept the government's contention that the full amount of depreciation and depletion *sustained*, whether allowable by law as a deduction from gross income in past years or not, must be deducted from cost in ascertaining gain or loss. Congress doubtless intended that the deduction to be made from the original cost should be the aggregate amount which the taxpayer was *entitled to deduct* in the several years" (Italics supplied).

Thus this Court has held in the total absence of provisions relating to adjustments on account of depreciation, that cost will be reduced only by the amount of the aggregate of depreciation which the taxpayer was entitled by law to deduct in determining net income for prior years. In the present case no depreciation was deductible by reason of the fact that the property was acquired and used for non-business purposes. The law was amended in 1924 to include a provision that depreciation should be deducted to the extent that it had been actually "allowed" as a deduction in prior years. The 1926 and 1928 Revenue Acts provided for an adjustment on account of the depreciation which was "allowable". Revenue Act of 1926, Section 202(b)(2); Revenue Act of 1928, Section 111(b)(2). This is in effect the rule as stated in the *Ludey* case. Later Acts required that cost be decreased on account of depreciation "allowed" but not less than depreciation "allowable". Revenue Acts of 1932 and 1934, Section 113(b)(1)(B). It is only for the *period prior to March 1, 1913*, that cost is reduced by depreciation actually *sustained* on the property. Revenue Acts of 1932 and 1934, Section 113(b)(1)(C).

Respondents respectfully submit that the rule as stated by this Court in the *Ludey* case in computing gain or loss

upon the sale of business property under the 1916 Law is equally applicable to computing the loss from a casualty to non-business property under the 1932 Law.

The property here was acquired *after* March 1, 1913. No depreciation was "allowed" or "allowable" and the taxpayer had no previous deduction on account thereof. Cost undiminished by physical depreciation or by subsequent fall in value constitutes the proper "basis" for measuring the deduction to which the respondents are entitled on account of the loss of property sustained.

Conclusion.

The Circuit Court of Appeals for the Second Circuit was correct in holding that the proper basis for measuring the deduction in the instant case was cost, and its judgment should be affirmed.

Respectfully submitted,

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SUPREME COURT OF THE UNITED STATES.

Nos. 180, 318.—October Term, 1938.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, 180 vs. Donald H. Owens and Marion Haviland Owens.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.
Amedeo Obici and Mrs. Amedeo Obici, Petitioners, 318 vs. Guy T. Helvering, Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

[January 3, 1939.]

Mr. Justice Roberts delivered the opinion of the Court.

The courts below have given opposing answers to the question whether the basis for determining the amount of a loss sustained during the taxable year through injury to property not used in a trade or business, and therefore not the subject of an annual depreciation allowance, should be original cost or value immediately before the casualty.[1] To resolve this conflict we granted certiorari in both cases.

In No. 180 the facts are that the respondent Donald H. Owens purchased an automobile at a date subsequent to March 1, 1913, and prior to 1934, for $1825, and used it for pleasure until June 1934 when it was damaged in a collision. The car was not insured. Prior to the accident its fair market value was $225; after that event the fair market value was $190. The respondents filed a joint income tax return for the calendar year 1934 in which they claimed a deduction of $1635, the difference between cost and fair market value after the casualty. The Commissioner reduced the deduction to $35, the difference in market value before and after the

[1] Helvering v. Owens, 95 F. (2d) 318; Helvering v. Obici, 97 F. (2d) 431.

collision. The Board of Tax Appeals sustained the taxpayers' claim and the Circuit Court of Appeals affirmed its ruling.

In No. 318 it appears that the taxpayers acquired a boat, boathouse, and pier in 1926 at a cost of $5,325. In August 1933 the property, which had been used solely for pleasure, and was uninsured, was totally destroyed by a storm. Its actual value immediately prior to destruction was $3905. The taxpayers claimed the right to deduct cost in the computation of taxable income. The Commissioner allowed only value at date of destruction. The Board of Tax Appeals held with the taxpayers but the Circuit Court of Appeals reversed the Board's ruling.

Decision in No. 180 is governed by the Revenue Act of 1934,[2] in No. 318 by the Revenue Act of 1932.[3] The provisions of both statutes touching the question presented are substantially the same and we shall refer only to those of the 1934 Act. Section 23(e)(3) permits deduction from gross income of losses "of property not connected with the trade or business" of the taxpayer, "if the loss arises from . . . casualty." Subsection (h) declares that "The basis for determining the amount of the deduction for losses sustained, to be allowed under subsection (e) . . . , shall be the adjusted basis provided in section 113(b)." Section 113 is entitled "Adjusted basis for determining gain or loss"; in subsection (a) it provides that "The basis of property shall be the cost of such property", with exceptions not material. Subsection (b), to which 23(h) refers, is: "*Adjusted basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided. (1) *General rule.*—Proper adjustment in respect of the property shall in all cases be made—(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws."

The income tax acts have consistently allowed deduction for exhaustion, wear and tear, or obsolescence only in the case of "property used in the trade or business." The taxpayers in these cases could not, therefore, have claimed any deduction on this account for years prior to that in which the casualty occurred. For this

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[2] c. 277, 48 Stat. 680, §§ 23 (e) (f) (h) (l), 24(a)1, 41, 113; 26 U. S. C. §§ 23, 24, 41, 113.

[3] c. 209, 47 Stat. 169, §§ 23 (e) (f) (g) (h), 24(a)1, 113.

reason they claim they may deduct upon the unadjusted basis,—that is,—cost. As the income tax laws call for accounting on an annual basis; as they provide for deductions for "losses sustained during the taxable year"; as the taxpayer is not allowed annual deductions for depreciation of nonbusiness property; as section 23(e)(3) requires that the deduction shall be on "the adjusted basis provided in section 113(b)", thus contemplating an adjustment of value consequent on depreciation; and as the property involved was subject to depreciation and of less value in the taxable year, than its original cost, we think section 113(b)(1)(B) must be read as a limitation upon the amount of the deduction so that it may not exceed cost, and in the case of depreciable non-business property may not exceed the amount of the loss actually sustained in the taxable year, measured by the then depreciated value of the property. The Treasury rulings have not been consistent, but this construction is the one which has finally been adopted.[4]

In No. 180 judgment reversed.
In No. 318 judgment affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

[4] Treasury Regulations 86, Arts. 23(e)-1, 23(h) 1, 113(b) 1; G. C. M. XV 1, Cumulative Bulletin 115-118.